MORTGAGE BULLETIN

PUBLISHED IN THE INTERESTS OF REAL ESTATE ANALYST SUBSCRIBERS BY

ROY WENZLICK & CO.

Real Estate Economists, Appraisers and Counselors

DECEMBER 17
1952

Volume XXI

Number 54

LENDERS WHISTLE WHILE BONES IN THE GRAVEYARD RATTLE

WE are almost at the threshold of a New Year which will bring problems of war and peace, personal security, integrity of the dollar, honesty in government, taxes, inflation and many other vexatious issues.

During the greater part of 1952, barring the depressed weeks of the steel strike, business has been good and the economy fairly well balanced - moving along a plateau. The business boom, now pretty well resumed, is tipping the scales upward and business activity is mounting and mounting fast. There is full employment and large production.

Fostered by a housing shortage, shifts in population and hyperemployment at increasingly higher wages, combined with an abundance of easy housing credit, this nation has experienced the biggest home-buying spree in history.

Millions of young couples with expanding families are hypothecating the next 15 to 20 years of their lives to the end that they may experience the pleasure and satisfaction of living in their own homes. The amortization of mortgage debt on liberal terms makes home ownership appear easy, but "easy" credit is never as easy as it looks.

With ample funds for mortgage investment on very liberal terms, the volume of mortgage financing has reached an exceedingly high level during recent years. G. Rowland Collins, dean of the Graduate School of Business of New York University, has designated the era through which we are passing as "the Golden Age of mortgage banking."

Bouncing back from the effects of the late steel strike, we are now in the midst of a resumed business boom which has helped to boost construction during the last quarter of the year and will continue to push up business generally through the spring months of 1953. There is, however, a dichotomy on the business outlook.

The American Bankers Association at its 78th annual convention expressed great uneasiness over future business conditions. Its advice to businessmen was to be cautious and not overconfident, as there is bound to be an interruption in business activity, perhaps by the end of the first quarter of 1953.

Several business analysts have already unfurled precautionary warnings of

stormy weather ahead. In a recent speech to the Investment Bankers annual convention in Hollywood, Florida, William McChesney Martin, Jr., chairman of the Federal Reserve Board, stated that the productive capacity of our country is so great that sooner or later prices will have to be reduced if we want to sell the goods.

The more optimistic among the builders and mortgage men, with their eyes fixed on the production of new dwelling units and the large volume of home mortgage recordings, seemingly are unaware of these warnings or choose to flout them. It is an old American cliche' that prosperity absorbs all criticism.

Possibly the high prices of real estate and continued good times will be with us as long as some real estate men can reassure prospective buyers. Possibly with our expanding economy we are in for a prolonged period of virtually full employment at increasingly higher wages. Possibly new home owners with slim equities will meet their mortgage payments without worry to themselves and the mortgagees. Possibly high-percentage loans, some of which are in nearly every portfolio, will turn out to be perfectly sound loans and not troublemakers. Possibly foreclosures and delinquencies will continue minimal. Possibly the new administration will increase interest rates on FHA and VA mortgages. Possibly the growing replacement market for homes, and the flow of existing families to the suburbs, will create a sufficient demand for new housing to offset the contraction in demand for new homes brought about by the decline in family formation. The stress, of course, is on the word "possibly."

But, again, it may be that this index of pleasant possibilities will prove incongruous and short-lived. If the log of the past is any guide, it would be forehanded to prepare for a period not too far distant, I imagine, when the capacity of the borrower to amortize his debt may be impaired, if not wholly dissipated, with the result that greater diligence will be called for on the part of the lenders to maintain their portfolios in sound and current condition.

Generally business is good. The production index is back to the April 1951 peak, and only two of every one hundred in the nation are jobless today; yet, paradoxically, perhaps, there is a widespread feeling among business observers that a recession will set in before the end of next year. Straws in the wind of seasoned opinion are blowing strongly in that direction.

Real estate has recently shown a rise in activity and housing starts are slightly ahead of the first 10 months of 1951. Nevertheless, with everything rosy, reports are drifting in from the convention of the National Association of Real Estate Boards at Miami which indicate there was a slight frostiness in the atmosphere of that sunny clime. While Realtors looked for plenty of business, many of them apparently felt that the big building boom is on the wane. Judging from the tales reported to have been tossed around among themselves, sales of houses from coast to coast are stickier than at any time since the war. Contingent on the section of the country Realtors told of sales sagging from 5 percent to 15 percent. Houses at $12,500 or less are active sellers, as they have been for months, but those in the $15,000 bracket and up are hard to move.

This confirms Roy Wenzlick's warning that the green light is going out and the amber light is flashing. He said traffic has not yet changed its direction but from now on the hazard is increasing. This is a period of grace which should be used to get in sound financial condition.

As recently as last October, Douglas Meredith, executive vice president of the National Life Insurance Company, told the Mortgage Bankers Association that our prosperity could come to an end at any time. "Because of the introduction of monthly payments to meet interest and mortgage charges, the purchase of a home today is virtually no more difficult than signing up for a new car, refrigerator or TV set." Mr. Meredith warned that the rapid expansion of home mortgage credit in recent years presents many acute problems for lenders and firms servicing housing loans. Any let-up in business conditions would spell ruin for companies not using foresight today. "We must remember," he asserted, "that Federal Reserve Board figures put the aggregate debt on one- to four-family houses on June 30 at $57 billion, nearly three times the $20 billion outstanding at the close of the boom in the twenties. And while there is much employment, income and wages are high and production great, some of us sense beneath the surface a hollowness which warns us that sooner or later the joy ride must end. . . The easy days won't last forever." In conclusion Mr. Meredith said, "Only a few present-day mortgage lenders and servicing agents can look back on the 'tough times' that came after the '29 crash. But, if we are realistic now, the impact of the decline won't hit so hard."

Techniques which have been successfully used in the booming, bustling market we have experienced in late years will be highly hazardous in the period ahead. The day has passed when a building can be built on the probability that it will turn out to be a paying investment. In recent years many a building, built with a high percentage mortgage, has proved to be sound, owing to later increases in construction costs and rising rentals. These circumstances increased the value of the property and at the same time shrank the mortgage. If the expected interruption in the boom occurs, the dollar will eventually gain in purchasing power. As the dollar increases in value, price distortions will tend to be corrected; i. e., prices which went up the most will tend to fall the most. If and when this happens, real estate will occupy a highly vulnerable position. This is so because the rise in building costs has been constantly advancing since the mid-thirties.

Our five-room brick veneer house, which would have cost $5,440 to build in St. Louis in 1939, costs $14,440 to build today. Our six-room frame house, which cost $5,671 to build in St. Louis in 1939, now costs $15,914 to build. To give you the change over a shorter span of time, our five-room brick veneer ranch house cost $12,000 to build in the suburbs in 1950 (national average); today the same house costs $13,830.

When these costs in 1939 are weighed against the current rate of construction, the present rate of family formation and the present carrying charges on houses already financed, the conclusions are disturbing to say the least.

Recently I sought the forthright opinion of an official of an out-of-New York savings bank which does $500,000 per month, or better, in home mortgage financing. I asked him to tell me what he thought of my guess that there would be an interruption in the boom in 1954 and, in all probability, the start of a recession. He replied he thought I was so right I could go out on that limb as far as I chose.

Then he continued: "The mortgage portfolio will be quite a headache. The home mortgage business is nothing more than a personal loan operation against a background of weekly salaries. Let employment slump and many of these 'shoe string' home owners will be only 60 to 90 days from the Sheriff's door. We are making most of our loans under the aegis of FHA insurance and VA guarantees. About 65 percent of all home mortgages are the conventional type where in effect the lender has to insure his own mortgages. I think these lenders will wind up owning some houses."

Despite the fact that the defense program is 6 to 8 months away from its peak, and that the present outlook is for a steady increase in employment in the months immediately ahead, there was more talk of an impending recession last week than there has been in several months. Elliot V. Bell, former superintendent of banks in New York State, is reported as saying: "Whether the boom lasts 6 months or 2 years more, the new Republican Administration will probably have to deal with a major business setback. On the other hand, most businessmen think a business recession is due in 1953 or 1954 but they do not expect it to be deep or disastrous."

The expectancy of this "interruption" is supported by considerable reinforcement from logic and experience, but as the factor of timing has always presented difficulties in making such guesses, the timing on this guess might be slightly off. However, an "interruption" in the business boom can be expected soon. Trees never reach the skies.

While one man's opinion may be as good as another's concerning a business recession, when once the swing is under way the individual businessman is about as potent to influence or direct it as a toad under a farmer's harrow.

One hundred years ago Thomas B. Macaulay, English historian, wrote his famous letter declaring that our American Government was all sail and no anchor and that it must eventually come to grief. The trends during the past twenty years might indicate he was right.

We hope the Republican Administration in its efforts to restore stability to the economy will not have too little sail and too much anchor.

E. G. Johnson

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